

demonstrate that the option position remains qualified will be similar to those currently in place for equity hedge exemptions. Currently a qualified account must report hedge information each time the option position changes. Hedge information for member firm and customer accounts are reported to the Exchange electronically, via the Large Options Position Report. Market maker account information is also reported to the Exchange electronically by the member's clearing firm. For those option positions that do not change, a filing is generally required on a weekly basis. Finally, the existing requirement imposed on member firms to report hedge information for proprietary and customer accounts that maintain an options position in excess of 10,000 contracts will remain in place.

The Exchange believes that all of the proposed qualified strategies are market neutral with the exemption of covered stock positions. According to the Exchange, we covered stock transactions (long stock/short call; short stock/short put) are not market neutral, the market exposure resides with the stock position where no limit is imposed. The Exchange believes that the short option premium mitigates the stock exposure and therefore no limit should be imposed on this strategy.

The Exchange believes that the proposed strategies do not lend themselves to market manipulation and should be exempt from position limits. The Exchange represents that the reporting requirements under PCX Rule 6.6 and internal surveillance procedures for hedged positions will enable the Exchange to closely monitor sizable option position and corresponding hedge.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,<sup>8</sup> in general, and furthers the objectives of Section 6(b)(5),<sup>9</sup> in particular, in that it is designed to promote just and equitable principles of trade and to protect investors and the public interest.

### *B. Self-Regulatory Organization's Statement on Burden on Competition*

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members's Participants, or Others*

Written comments were not solicited or received with respect to the proposed rule change.

### **III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission will:

(A) By order approve such proposed rule change, or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposal is consistent with the Act. The Commission is especially interested in receiving written, data, views and arguments concerning the use of a listed option position hedged on a one-for-one basis with an OTC option position on the same underlying security. In particular, the Commission staff has concerns that such exemption would grant members the ability to sell OTC options and hedge such positions on the exchange with listed options on an unlimited basis. This potentially raises manipulation concerns. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 522, will be available for inspection and copying in the Commission's Public Reference Room, 450 Fifth Street, NW., Washington, DC 20549-0609. Copies of such filing will also be available for inspection and copying at the principal office of the PCX. All submissions should refer to File No. SR-PCX-00-45

and should be submitted by September 7, 2001.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>10</sup>

**Margaret H. McFarland,**  
*Deputy Secretary.*

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## **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-44672; File No. SR-Phlx-2001-67]

### **Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment Nos. 1 and 2 by the Philadelphia Stock Exchange, Inc. Relating to Automatic Price Improvement for Equities Trading in Decimals**

August 9, 2001.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on July 24, 2001, the Philadelphia Stock Exchange, Inc. ("Phlx" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. On August 7, 2001, the Exchange amended the proposal.<sup>3</sup> The Exchange filed another amendment on August 9, 2001.<sup>4</sup> The Exchange filed this proposal under section 19(b)(3)(A) of the Act,<sup>5</sup> and Rule 19b-(f)(6)<sup>6</sup> thereunder, which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule

<sup>10</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See August 6, 2001 letter from Jurij Trypupenko, Esquire, Phlx to Alton S. Harvey, Division of Market Regulation ("Division"), Commission and attachments ("Amendment No. 1"). In Amendment No. 1, the Phlx clarified that the only proposed substantive change to the pilot program was to extend its operation through November 5, 2001. Amendment No. 1 also provided a clear explanation of proposed technical changes to rule language to conform the language to prior filings.

<sup>4</sup> See August 8, 2001 letter from Jurij Trypupenko, Esquire, Phlx to Alton S. Harvey, Division, Commission ("Amendment No. 2"). In Amendment No. 2, the Phlx amended the proposed rule language to clarify that the pilot will operate through November 5, 2001.

<sup>5</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>6</sup> 17 CFR 240.19b-4(f)(6). The Phlx requested that the Commission waive the 5-day prefiling notice requirement, and the 30-day operative delay.

<sup>8</sup> 15 U.S.C. 78f(b).

<sup>9</sup> 15 U.S.C. 78f(b)(4).

change, as amended, from interested persons.

### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to extend through November 5, 2001 its Philadelphia Stock Exchange Automated Communication and Execution System ("PACE")<sup>7</sup> price improvement pilot program ("pilot program"). The pilot program, which is found in Supplementary Material .07 to Phlx Rule 229, has an automated price improvement feature based on a percentage of the spread between the bid and the offer. The current pilot program, established in SR-Phlx-2001-12, has been in effect since January 29, 2001.<sup>8</sup>

The only substantive change the Phlx proposes at this time is to extend the pilot program through November 5, 2001.

The remaining changes proposed at this time are non-substantive formatting and language changes. These are cosmetic changes to ensure that the pilot program reflects amendments that were made in previous filings that were inadvertently overlooked. The underscored proposed language was added in SR-Phlx 00-54,<sup>9</sup> but mistakenly did not appear in SR-Phlx-2001-12,<sup>10</sup> and is therefore noted as additional language at this time. The bracketed language (except as noted below) was deleted by SR-Phlx-00-54, but mistakenly appeared in SR-Phlx-2001-12. It is now noted as deleted language to correct this mistake. The final bracketed phrase, which begins ".03 or greater," appeared in SR-Phlx-00-54. It was mistakenly included in SR-Phlx-2001-12, and is therefore noted now as deleted language.<sup>11</sup>

The Exchange recognizes that all options currently trade in decimals, and is proposing the non-substantive language changes herein to conform the language of Phlx Rule 229 to prior filings. The following is the text of the

proposed rule change. Additions are in *italics*. Deletions are in brackets.

### Rule 229. Philadelphia Stock Exchange Automated Communications and Execution System (PACE)

PACE provides a system for the automatic execution of orders on the Exchange equity floor under predetermined conditions. Orders accepted under the system may be executed on a fully automated or manual basis in accordance with the provisions of this Rule. Securities admitted to dealings on the equity floor are eligible for trading on the PACE System in which equity specialists and member organizations may choose to participate. The conditions under which orders will be accepted and executed are set forth below. When used in the Rule, PRL means a combined round-lot and odd-lot order, and PACE Quote means the best bid/ask quote among the American, Boston, Cincinnati, Chicago, New York, Pacific or Philadelphia Stock Exchange, or the Intermarket Trading System/Computer Assisted Execution System ("ITS/CAES") quote, as appropriate. The PACE rules, conditions and guidelines do not apply to orders not on the system, and existing rules governing orders not on the system are not affected hereby.

#### Supplementary Material:

##### General

\* \* \* \* \*

.07

\* \* \* \* \*

(c) Price Improvement for PACE Orders  
(i) Automatic Price Improvement—Where the specialist voluntarily agrees to provide automatic price improvement to all customers and all eligible market orders in a security, automatically executable market and marketable limit orders in New York Stock Exchange and American Stock Exchange listed securities received through PACE for 599 shares or less shall be provided with automatic price improvement from the PACE Quote when received of  $\frac{1}{16}$  (or  $\frac{1}{64}$  in the case of Nasdaq-100 Index Tracking Stock) for equities trading in fractions or, either \$.01 or a percentage of the PACE Quote when the order is received for equities trading in decimals beginning at 9:30 A.M., except where:

(A) a buy order would be improved to a price less than the last sale or a sell order would be improved to a price higher than the last sale (except as provided in (E) below); or

(B) a buy order would be improved to the last sale price which is a downtick or a sell order would be improved to the last sale price which is an uptick (except as provided in (E) below). The PACE System will determine whether the last sale price is a downtick or an uptick. The PACE System does not recognize changes from the previous day's close. In these situations, the order is not eligible for automatic price improvement,

and is, instead, automatically executed at the PACE Quote.

A specialist may voluntarily agree to provide automatic price improvement to larger orders in a particular security to all customers under this provision.

A specialist may choose to provide automatic price improvement for equities trading in fractions where the PACE Quote is (I)  $\frac{3}{16}$  or greater, (II) [or]  $\frac{1}{8}$  or greater, or (III) solely with respect to Nasdaq-100 Index Tracking Stock <sup>SM</sup>,  $\frac{1}{16}$  or greater. [for equities trading in fractions:] For equities trading in decimals, a specialist may choose to provide automatic price improvement of (i) \$.01 where the PACE Quote is [.03 or greater or .05 or greater for equities trading in decimals] either \$.05 or greater, or \$.03 or greater, or (ii) where the PACE Quote is \$.02 or greater, a percentage of the PACE Quote when the order is received, up to 50%, rounded to the nearest penny, and at least \$.01, in a particular security to all customers.

\* \* \* \* \*

.21 The automatic price improvement feature based on a percentage of the spread between the bid and offer in Supplementary Material .07(c)(i) will be in effect for a pilot period through November 5, 2001.

\* \* \* \* \*

### II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

#### A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

##### 1. Purpose

The Phlx proposes to extend, through November 5, 2001, the Phlx's pilot program that incorporates automatic price improvement for equities trading in decimals based on a percentage of the spread between the bid and offer.<sup>12</sup> In addition to extending the date of the pilot program, the proposed rule change

<sup>7</sup> PACE is the Exchange's automated order delivery, routing, execution and reporting system for equities.

<sup>8</sup> See Securities Exchange Act Release No. 43901 (January 30, 2001), 66 FR 8988 (February 5, 2001).

<sup>9</sup> See Securities Exchange Act Release No. 43717 (December 13, 2001) 65 FR 80976 (December 22, 2000) (SR-Phlx-00-54).

<sup>10</sup> See footnote 7, *supra*.

<sup>11</sup> The Phlx intends to file a proposed rule change in the future to remove references to fractional pricing from this and other rules.

<sup>12</sup> See Securities Exchange Act Release No. 43901 (January 30, 2001), 66 FR 8988 (February 5, 2001) (SR-Phlx-2001-12) (implementation of pilot program).

makes non-substantive cosmetic changes to correct the inaccuracies in the rule language inadvertently made in previous proposed rule changes.

## 2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with section 6 of the Act<sup>13</sup> in general, and in particular, with section 6(b)(5),<sup>14</sup> in that it promotes just and equitable principles of trade, fosters cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitates transactions in securities, removes impediments to and perfects the mechanism of a free and open market and a national market system, and, in general, protect investors and the public interest by widely extending automated price improvement to equities traded in decimals.

### *B. Self-Regulatory Organization's Statement on Burden on Competition*

The Exchange does not believe that the proposed rule change will impose any inappropriate burden on competition.

### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others*

No written comments were either solicited or received.

## III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not:

- (i) significantly affect the protection of investors or the public interest;
- (ii) impose any significant burden on competition; and
- (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to section 19(b)(3)(A) of the Act<sup>15</sup> and Rule 19b-4(f)(6) thereunder.<sup>16</sup> At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.<sup>17</sup>

The Exchange has requested that the Commission finds good cause to waive the pre-filing notice requirement, and to designate the proposal to be both effective and operative upon filing because such designation is consistent with the protection of investors and the public interest. Waiver of these requirements will allow the pilot program to continue uninterrupted through November 5, 2001. For these reasons, the Commission finds good cause to designate that the proposal is both effective and operative upon filing with the Commission.<sup>18</sup>

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposal is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of the exchange. All submissions should refer to file number SR-Phlx-2001-67, and should be submitted by September 7, 2001.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>19</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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have commenced on August 7, 2001, the date the Phlx filed Amendment No. 1.

<sup>18</sup> For purposes only of accelerating the operative date of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>19</sup> 17 CFR 200.30-3(a)(12).

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-44687; File No. SR-Phlx-2001-58]

### **Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto by the Philadelphia Stock Exchange, Inc. Establishing Obligations of AUTOM Order Entry Firms and Users and Prohibiting Entry of Multiple Orders Via AUTOM for the Account(s) of the Same Owner of Beneficial Interest for the Same Option Within 15 Seconds**

August 13, 2001.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4<sup>2</sup> thereunder, notice is hereby given that on June 8, 2001, the Philadelphia Stock Exchange, Inc. ("Exchange" or "Phlx") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Phlx. On July 13, 2001, the Phlx submitted Amendment No. 1 to the proposed rule change.<sup>3</sup> The proposed rule change, as amended, has been filed by the Phlx as a "non-controversial" rule change under Rule 19b-4(f)(6)<sup>4</sup> under the Act. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

### **I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change**

The Phlx proposes to amend Exchange Rule 1080, Philadelphia Stock Exchange Automated Options Market ("AUTOM") and Automatic Execution System ("AUTO-X"),<sup>5</sup> to define an

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See letter from Edith Hallahan, First Vice President & Deputy General Counsel, Phlx, to Nancy Sanow, Assistant Director, Division of Market Regulation ("Division"), Commission, dated July 12, 2001 ("Amendment No. 1"). In Amendment No. 1, Phlx made a change to the proposed rule language. Specifically, Phlx removed the word "issue" from Phlx Rule 1080(c)(ii)(B)(3). For purposes of calculating the 60-day period within which the Commission may summarily abrogate the proposed rule change under Section 19(b)(3)(C) of the Act, the Commission considers that period to commence on July 13, 2001, the date the Phlx filed Amendment No. 1. See 15 U.S.C. 78s(b)(3)(C).

<sup>4</sup> 17 CFR 240.19b-4(f)(6).

<sup>5</sup> AUTOM is the Exchange's electronic order delivery and reporting system, which provides for the automatic entry and routing of equity option and index option orders to the Exchange trading floor. Orders delivered through AUTOM may be executed manually, or certain orders are eligible for

Continued

<sup>13</sup> 15 U.S.C. 78f.

<sup>14</sup> 15 U.S.C. 78f(b)(5).

<sup>15</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>16</sup> 17 CFR 240.19b-4(f)(6).

<sup>17</sup> For purposes of calculating the abrogation date, the Commission considers the 60-day period to